SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Assm. Rev. & Tax Comm. Analyst: Jeff Garnier Bill Number: AB 1208

Related Bills: AB 2797 (1998) Telephone: 845-5322 Amended Date: 6-29-99 & 7/1/99

Attorney: Patrick Kusiak Sponsor:

SUBJECT: Conformity Act of 1999

____	DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.
X	AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
____	AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _____.
____	FURTHER AMENDMENTS NECESSARY.
X	DEPARTMENT POSITION CHANGED TO Support.
X	REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED 6/17/99STILL APPLIES.
____	OTHER - See comments below.

SUMMARY OF BILL

The Personal Income Tax Law (PITL) and the Bank and Corporation Tax Law (B&CTL), in general, conform to the Internal Revenue Code (IRC) either by incorporating the IRC by reference as of a "specified date" or by stand alone language which mirrors the federal provision. California law is conformed to the IRC as of January 1, 1998, unless a specific provision provides otherwise. This bill would change the specified date from January 1, 1998, to January 1, 1999, for taxable and income years beginning on or after January 1, 1999. Changing the specified date automatically conforms to all changes from January 1, 1998, through December 31, 1998, to IRC sections that have been previously incorporated by reference. Thus, California law would conform to numerous changes made to federal income tax law by the IRS Restructuring and Reform Act of 1998 and certain other federal acts enacted during 1998.

This bill also would make numerous changes to specifically not conform to particular federal provisions or to modify the general conformity to certain items in the IRC. Additionally, numerous technical changes regarding cross references and the deletion of unnecessary language that was used to conform to federal law changes subsequent to January 1, 1998, and prior to January 1, 1999, are being made by this bill.

Additionally, this bill also contains two of the department's legislative proposals: "Repeal of Capital Loss Limitation and Carryover Provisions for Corporations" and "Revise the LLC Annual Franchise Tax Due Date to the Date of Return."

Board Position:			Department/Legislative Director	Date
___X___ S	_____ NA	_____ NP		
_____ SA	_____ O	_____ NAR		
_____ N	_____ OUA	_____ PENDING	**Johnnie Lou Rosas**	**7/16/1999**

SUMMARY OF AMENDMENTS

The June 29, 1999, amendment made the following changes:

- Prior to the June 29, 1999, amendment, the bill would have conformed the B&CTL to federal section 179 rules regarding the expensing of assets, but limited the deduction amount to $17,000 per year (current federal and PITL amount is $19,000.) The amendment would conform the B&CTL to the federal section 179 deduction rules and amounts (item 13).
- The amendment would repeal the capital loss limitation and carryover provision for corporations (item 14).
- The amendment would create a rebuttable presumption for possession corporations that elect the profit split method under Section 936 of the Internal Revenue Code (IRC) that the allocation of combined taxable income under the profit split method is a proper allocation under the principles of Section 482 of the IRC (transfer-pricing) (item 15).
- Removed language that would have conformed the PITL to the federal self-employed health insurance deduction phase-in percentages. (This provision was enacted by AB 1289 (St. 1999, Ch. 117).)
- Made four technical changes affecting cross references and grammar.
- The amendment also added language affecting the interest rate charge on Sales and Use Taxes not timely paid. This analysis does not address this provision.

The July 1, 1999, amendment added a provision, sponsored by the Franchise Tax Board, that would make the annual tax of a limited liability company (LLC) classified as a partnership, or whose entity status is disregarded, due and payable on the due date of the LLC return.

EFFECTIVE DATE

Unless otherwise specified, this bill would apply to taxable and income years beginning on or after January 1, 1999.

SPECIFIC FINDINGS

This bill would make changes affecting the following areas:

1. Deductibility of Meals Provided for the Convenience of the Employer.
2. Employer Deductions for Vacation and Severance Pay.
3. Certain Trade Receivables Ineligible for Mark-To-Market Treatment.
4. Exclusion of Minimum Required Distrib. from AGI for Roth IRA Conversions.
5. Farm Production Flexibility Contract Payments
6. Treatment of Certain Deductible Liquidating Distrib. of RICs and REITs.
7. Tax Treatment of Cash Options for Qualified Prizes.
8. Exclusion from Income for Employer-Provided Transportation Benefits.
9. Payments Received Pursuant to the Ricky Ray Hemophilia Relief Fund Act.
10. Waiver of estimated tax penalty.
11. 1998 Federal Technical Changes.
12. Provision removed by June 29, 1999, amendment.
13. Election to Expense the Cost of Certain Depreciable Assets Permitted Under the B&CTL.

14. Repeal of Capital Loss Limitation and Carryover Provisions for Corporations.
15. Profit Split Method for Computing Income for Corporations Filing Combined Reports.
16. Revise LLC Annual Franchise Tax Due Date to Date of Return.

Except for item 12, the self-employed health insurance deduction, the modification to item 13, expensing of assets (Section 179 deduction for corporations) and the addition of items 14, 15 and 16 the May 28, 1999, revised analysis still applies.

13. Election to Expense the Cost of Certain Depreciable Assets Permitted Under the B&CTL.

Federal law and PITL provides that in lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment in depreciable assets may elect to currently deduct, rather than capitalize and depreciate, up to $19,000 of the cost of qualifying property placed in service in a taxable year beginning after December 31, 1998. In general, qualifying property, commonly referred to as section 179 property, is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business.

The limitation amount is reduced (but not below zero) by the amount by which the cost of section 179 property placed in service during the taxable year exceeds $200,000.

In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income of the taxpayer for the year that is derived from the active conduct of any trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to similar limitations).

The **federal and PITL** expense amount increases from $19,000 to $25,000. The increase is phased in as follows:

Taxable year beginning in-	Maximum expensing
1999	$19,000
2000	$20,000
2001 and 2002	$24,000
2003 and thereafter	$25,000

This bill would conform the California B&CTL to federal section 179 deduction.

FISCAL IMPACT

Departmental Costs

This provision would not significantly impact the department’s costs.

Tax Revenue Estimate

Based on federal estimates, the revenue loss for this provision is -$36 million, -$28 million and -$27 million for fiscal years 1999-00, 2000-01 and 2001-02, respectively. Prior to the June 29, 1999, amendment the bill would have conformed to the federal Section 179 property deduction but limited the deduction to $17,000 per year. The estimated revenue loss from the provision prior to the June 29, 1999, amendment was -$32 million, -$23 million and -$17 million for fiscal years 1999-00, 2000-01 and 2001-02, respectively.

14. Repeal of Capital Loss Limitation and Carryover Provisions for Corporations

State law generally conforms to federal law relating to the computation of gain or loss on the disposition of capital assets.

Federal law (IRC Section 1221) provides that capital assets are property other than: stock in trade or other inventory-type property held primarily for sale to customers; depreciable or real property used in a trade or business; patents held as inventory, copyrights and other literary property; accounts or notes receivable acquired in the ordinary course of business; and U.S. government publications, as specified.

Generally, capital gain is realized and recognized when a capital asset is sold or exchanged and the amount realized exceeds the basis of the asset and the amount subject to recapture under federal law. Basis in a capital asset is determined by the cost of the asset and is increased by further investment or decreased by allowable deductions. Capital loss occurs when a capital asset is sold or exchanged and the amount realized is less than the basis of the asset. Generally, any gain or loss from the sale or other disposition of property that does not qualify as a capital asset is ordinary gain or loss.

IRC Section 1231 gains and losses arise from certain dispositions of Section 1231 property. Section 1231 gains are gains from (1) the sale or exchange of depreciable personal or real property used in a trade or business (not mere investment) and held for more than one year and (2) the conversion of business or investment property held for more than one year. Section 1231 losses are losses from the sale or exchange or conversion of business or investment property held for more than one year. Generally, if Section 1231 gains exceed Section 1231 losses, the net gains are treated as long-term capital gains. If Section 1231 losses exceed Section 1231 gains, the losses are ordinary losses. Section 1231 gains must be treated as ordinary income to the extent of the taxpayer’s Section 1231 losses in the preceding five years.

Federal law (IRC Section 1222) provides rules relating to the netting of capital gains and losses. Short-term capital gains are netted with short-term capital losses to arrive at net short-term capital gains/losses. Long-term capital gains are netted with long-term capital losses and net Section 1231 gains to arrive at net long-term capital gains/losses. Net short-term capital gains/losses and net long-term capital gains/losses are netted. If a net gain results, then that gain is included in income. If a net loss results, it is not currently deductible for corporations, or up to $3,000 may be deductible for individuals.

Under current **federal and state law**, corporations may deduct capital losses only to the extent of capital gains. **Federal law** generally permits a three-year carry-back and a five-year carry-forward for excess capital losses. **State law,** however, permits only a five-year carry-forward for excess capital losses.

Under current **federal law**, the generally applicable maximum rate on corporate ordinary income is 35%, and the tax on net capital gains for corporations is limited to a maximum rate of 35%. Under current **state law**, capital gains for corporate taxpayers are taxed at the same rates as ordinary income (8.84%), with no maximum capital gain rate.

In 1990, **California law** adopted the federal statutes concerning capital loss limitations and made no modifications to address combined report issues. The federal law is based on a single entity approach. However, federal regulations provide special rules for federal consolidated returns so the capital loss limitation is applied on a group basis. Since California law does not conform to the federal consolidated return provisions, the federal regulations relating to consolidated returns do not apply.

The **California law** regulations for Section 25106.5, relating to combined reporting, provide for the intrastate apportionment of business gains or losses from the sale or exchange of capital assets, Section 1231 property and involuntary conversions prior to the IRC Section 1221 capital gain/loss netting provisions. Those gain/loss items are then netted at the entity level after intrastate apportionment.

This bill would repeal the capital loss limitation and carryover provision for corporations for income years beginning on or after January 1, 1999. Capital loss carryover amounts from income years beginning before January 1, 1999, would continue under the current rules (i.e., capital losses may be deducted only to the extent of capital gains and excess capital losses may be carried forward for five years).

Allowing the deduction of the current year’s capital loss would return California law to the way it was prior to the conformity to the federal capital loss limitation rules.

Policy Considerations

- This provision could cause a taxpayer to lose as much as half of the capital loss amount if the taxpayer has an overall loss for the year the capital loss is recognized since the carryover would be subject to California's general net operating loss rules, which generally permit only 50% of an operating loss to be carried forward (subject to certain exceptions not relevant herein). In contrast, under current law, 100% of the excess capital loss would be carried forward and could be absorbed in future years if the taxpayer had sufficient capital gains within the succeeding five years.

- In general, tax treatment of various items under the Personal Income Tax Law (PITL) and Bank and Corporation Tax Law (B&CTL) are consistent. This provision would make the treatment of capital losses different under the PITL and B&CTL. However, there are currently differences between PITL and B&CTL treatment of capital losses, as well as with respect to certain capital gains (e.g., qualified small business stock rules apply only to PITL taxpayers).

Departmental Costs

This provision would not significantly impact the department's costs.

Tax Revenue Estimate

This provision would result in the following order of magnitude losses in the initial three fiscal years.

Effective For Dispositions in Income Years BOA 1/1/99 [$ In Millions]			
	1999-00	2000-01	2001-02
Repeal of Capital Loss Limitation	($5)	$1	$3

The second and third fiscal year impacts allow for revenue savings from reduced carryover losses. The drop-off effect for this provision is rather pronounced due to recharacterizing all unapplied losses for the 1999-00 fiscal year as net operating losses subject to a 50% carryover rather than a 100% capital loss carryover.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

The impact reflects the additional amount of losses that are applied for the year, combined with reduced loss carryovers to subsequent years.

This provision would allow any capital loss be applied against all positive income of a corporation. Any remaining losses would be carried over to subsequent years at 50% as a net operating loss. Tax return data (state or federal) regarding total corporate capital losses reported in any given year and amounts applied and unapplied are not available. Based on the judgment of both audit and legal staff, this proposal would not significantly increase revenue losses and additionally would generate revenue savings in subsequent years based on the difference in carryovers (a 50% carryover rather than 100% for unapplied losses). In a number of cases examined for significant corporations, total capital gains within the unitary group have been of sufficient magnitude to absorb most capital losses.

15. Profit Split Method for Computing Income for Corporations Filing Combined Reports.

Under current federal law, corporations organized in the United States (U.S.) are taxed on all their income, regardless of source, and are generally allowed a credit for any taxes paid to a foreign country on their foreign source income.

Under current federal law, foreign corporations engaged in an U.S. trade or business are taxed at regular progressive U.S. rates on income effectively connected with the conduct of that business in the U.S. This is known as effectively connected income or ECI. However, foreign corporations are taxed at a flat 30% rate (or lower rate if provided by treaty) on certain income (usually investment income) from U.S. sources.

Federal law uses the "separate accounting method" to determine the amount of a corporation's income subject to tax. The separate accounting method determines the income of related corporations on a corporation-by-corporation basis and does not take into consideration the income of related corporations not subject to tax within the taxing jurisdiction.

The separate accounting method is generally premised upon the use of "arm's-length" pricing in transactions between related parties. Under this principle, the prices or charges on transactions between related parties should be the same as if the transactions occurred between unrelated parties. However, in many situations related corporations may realize an overall tax benefit for the affiliated group by shifting income between affiliates and not charging an "arm's-length" price.

Internal Revenue Code (IRC) Section 482 was enacted to prevent any arbitrary shifting of income between affiliates. The Internal Revenue Service (IRS) conducts Section 482 audits to determine if the related parties have charged an "arm's-length" price and, if not, what the "correct" price should be. This is commonly referred to as transfer pricing.

Under federal law, in determining the Puerto Rico and possession tax credit, a possession corporation[1] may elect to attribute some of the income from intangible property[2] to the U.S. corporation by use of either the cost sharing method or the profit split method. If neither method is elected, virtually all of the income attributable to the intangible property is considered U.S. source income. Thus, a possession corporation is treated as a contract manufacturer not owning any intangible property, even if the intangible property was purchased from unrelated parties or developed by the possession corporation itself.

The Puerto Rico and possession tax credit is terminated for tax years beginning after December 31, 1995. However, special phase-out rules apply in the case of existing credit claimants. Existing credit claimants may continue to claim the credit throughout the last tax year beginning before January 1, 2006. For tax years beginning in 2006 and thereafter, the credit is scheduled to expire.

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[1] Possessions corporations are U.S. incorporated entities located in U.S. possessions, most notably Puerto Rico, which have elected the benefits of Internal Revenue Code Section 936.

[2] Intangible property includes patents, inventions, copyrights, trade names and trademarks.

If the cost sharing method is elected for **federal purposes**, the possession corporation is required to pay its affiliates for its share of product research and development costs incurred by the affiliates during the year. The cost share payment cannot be less than the cost share payment that would be required under IRC Section 482.

If the profit split method is elected for **federal purposes**, the taxpayer is permitted to arbitrarily attribute 50% of the manufacturing profits (for the product lines covered by the profit spit method) to the possession corporation. If the federal profit split amount reportable by the possession corporation is less than the amount of net income reported by the possession corporation on its books, the possession corporation will usually remit a payment to the U.S. shareholder. If the reverse occurs, the U.S. parent corporation remits a payment to the possession corporation. Procedurally, the IRS does not conduct Section 482 audits of corporations electing the profit split method in determining the Puerto Rico and possession tax credit and treats that method as properly reflecting the income of the electing corporation.

Under current California law, California source income for corporations that operate both within and without the state is determined using the unitary method of taxation. Under the worldwide unitary method, the income of related affiliates that are members of a unitary business is combined to determine the total income of the unitary group. A share of that income is then apportioned to California on the basis of relative levels of business activity in the state, as measured by property, payroll, and sales. The fundamental difference between the worldwide unitary method and the federal separate accounting method discussed above is that the prices or charges on transactions between related parties are simply disregarded under the unitary method, as opposed to adjusted under separate accounting rules.

As an alternative to the worldwide unitary method, **California law** allows corporations to elect to determine their income on a "water's-edge" basis. Water's-edge electors generally can exclude unitary foreign affiliates from the combined report used to determine income derived from or attributable to California sources. Therefore, in a water’s-edge combined report, the allocation of income between affiliated corporations, some of whom are members of the water's-edge group and some of whom are not, is relevant to the correct determination of income from California sources.

Generally possessions corporations are excluded from the water's-edge combined report group, unless:

- the possessions corporation's average United States factor is equal to 20% or more; or
- the possessions corporation earns U.S. source income which is effectively connected with a U.S. trade or business, and if the possessions corporation is considered a taxpayer for California purposes.

California law requires the department to conduct transfer-pricing audits (Section 482 audits) to ensure that taxpayers include the correct amount of income in the water’s-edge combined report. The department is not required to perform an audit if the IRS is examining the taxpayer for the same year or years on the same issues. If the IRS does conduct a detailed Section 482 audit, **California law** specifies that it shall be presumed correct and that the results of the federal audit apply for state tax purposes. This presumption can be overcome if either the FTB or the taxpayer demonstrates that:

- An adjustment or the failure to make an adjustment was erroneous.
- The results of such an adjustment would produce a minimal tax change for federal purposes because of correlative or offsetting adjustments or for other reasons.
- Substantially the same federal tax result was obtained under other IRC sections.

If the IRS does not conduct a Section 482 audit of any particular taxpayer, **California law** specifies that no inference shall be drawn for state purposes from this failure.

California law does not conform to the IRC Section 936 elections relating to the profit sharing or profit split methods used in computing the federal Puerto Rico and possessions tax credit. For **California purposes**, IRC Section 482 governs the relationship between a possession corporation and the U.S. affiliates.

This provision of the bill would create a rebuttable presumption for possession corporations that elect the profit split method under Section 936 of the IRC that the allocation of combined taxable income under the profit split method is a proper allocation under the principles of Section 482 of the IRC (transfer-pricing). Thus, **this bill** would essentially allow use of the profit split method for California purposes. This provision of the bill is doubled joined to SB 1229 to prevent chaptering problems.

Policy Considerations

- Section 482 (transfer-pricing) audits are very resource-intensive and taxpayer intrusive. For this reason, California is not required to conduct a Section 482 audit if the IRS has conducted such an audit. Presuming that the profit split method elected under federal law (IRC Section 936) provides the correct value under Section 482, this provision would reduce the number of Section 482 audits the department is required to conduct.

- The profit split method will sometimes assign substantially more income to the possession corporation than would be assigned under a Section 482 (transfer-pricing) method. In such cases, the rebuttable presumption would allow the state to allocate income under Section 482 to clearly reflect the income attributable to members of the water's-edge group.

Department Costs

To the extent that this bill simplifies or reduces transfer pricing audits and reduces disputes between taxpayers and the department, cost savings for the department’s audit and legal staff may result. The extent of these possible savings cannot be quantified.

Tax Revenue Estimate

Based on limited data and assumptions discussed below, this provision would result in the following revenue losses.

Estimated Revenue Impact of Profit Split Method [$ In Millions]					
1999-00	2000-01	2001-02	2002-03	2003-04	2004-05
-$1	-$3	-$2	-$2	-$1	-$1

This provision would be effective January 1, 1999, and would apply to all years for which the statute of limitation is still open.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

Revenue losses from audits not undertaken would determine the revenue impact of this provision. If, under this provision, Section 936 profit splitting rules were presumed to satisfy Section 482 transfer-pricing requirements (subject to rebuttal on audit), some audits would not be initiated if a preliminary analysis suggests a final result in the range of a 50/50-profit split.

To quantify the potential revenue effects of not pursuing certain audits under this proposal, otherwise likely audit assessments were approximated and grown 5% per year. For subsequent years, losses are phased out to reflect the sunset of Section 936 for taxable years beginning after December 31, 2005. Estimated losses reflect the projected cash flow impact of reduced taxes plus any applicable interest for the initial six fiscal years beginning in 1999-00.

16. Revise LLC Annual Franchise Tax Due Date to Date of Return.

Background

The Business Entities Section of the department’s Processing Services Bureau conducted a study of 500 randomly selected LLC returns (CA Form 568) for tax years 1995 and 1996. The study found that 73% of the returns contained errors related to the payment of tax: either no annual tax was paid, or the tax was paid with the return rather than with the required form FTB 3522 on or before the 15th day of the fourth month of the taxable year. The error rate appears to be declining as educational programs are implemented; however, the error rate is still high, as is the growth in LLC formations (approximately 1,500 – 2,000 per month). The LLC Interim Billing Project is billing late paying LLCs for current year annual tax, annual fee, interest, and penalties. The first bills were sent in late August 1998. Bills continue to be sent out. As of January 22, 1999, approximately 8,800 of the nearly 15,000 billing notices had been sent out with balances totaling approximately $416,500.

Under federal law, a business entity (other than a “corporation per se”) is an “eligible entity” and may elect its classification for tax purposes. An LLC is

an eligible business entity and may be treated and taxed under federal law as a corporation, a partnership, or entirely disregarded as a separate entity. Fewer than 25 of approximately 40,000 LLCs in California are classified as corporations.

California law adopted federal law concerning the classification of business entities for tax purposes, with some minor modifications. In particular, the tax and fee previously imposed on an LLC classified as a partnership now apply to any LLC not classified as a corporation, including an LLC that is otherwise disregarded for federal and state tax purposes. In general, the classification of a business entity in California must be the same as its federal classification.

Existing state law imposes on a corporation doing business in this state a tax to be paid annually for the privilege of exercising its corporate franchise within this state. The tax is the greater of the minimum franchise tax, currently $800 (certain qualifying new corporations pay a reduced amount), or the tax according to or measured by its net income computed at the current rate of 8.84%. For the first taxable year, the minimum franchise tax is paid to the Secretary of State (SOS) with the filing of the articles of incorporation. For a corporation deriving income from California sources (but not doing business in this state), the tax rate also is 8.84%, but the corporation is not required to pay the minimum franchise tax.

Existing state law requires individuals and corporations to have taxes withheld or make estimated tax payments throughout the taxable or income year. In the case of corporations, the first estimated tax payment, due by the 15th day of the fourth month after the beginning of the income year, must be an amount at least equal to the minimum franchise tax ($800).

Under current state law, a foreign or domestic LLC classified as a partnership or disregarded for tax purposes that is doing business in this state is required to annually pay a tax and a fee. The annual tax is for the privilege of doing business in this state; the amount is equal to the minimum franchise tax. The annual fee is determined by the amount of total income of the LLC from all sources reportable to this state.

Existing state law requires the tax on LLCs to be paid on or before the 15th day of the fourth month of the taxable year. The FTB provides the LLC tax voucher form FTB 3522 for this remittance.

Existing state law requires the fee of an LLC to be paid on the date the return for the LLC is required to be filed. The return for an LLC classified as a partnership is due on or before the 15th day of the fourth month after the close of the taxable year. The return for an LLC that is disregarded is due on or before the 15th day of the fourth month after the close of the taxable or income year of the owner of the disregarded LLC.

Existing state law requires limited partnerships (LPs) and limited liability partnerships (LLPs) formed, registered, or doing business in this state, to annually pay a tax for the privilege of doing business in this state. The amount of this annual tax is equal to the minimum franchise tax. This tax is due and payable on the date the return of the LP or LLP is required to be filed, the 15th day of the fourth month after the end of the taxable year. However, unlike LLCs, LPs and LLPs are not otherwise taxable or subject to additional fees.

This bill would make the annual tax of an LLC classified as a partnership or whose entity status is disregarded due and payable on the due date of the LLC return, rather than on the 15th day of the fourth month of the LLC's taxable year. This provision is effective for taxable years beginning on or after January 1, 2000.

Policy Considerations

By making the timing of the payment of LLC tax similar to taxes paid by LPs and LLPs, this bill would result in greater simplicity for both taxpayers and the department by making the calculation, payment, and administration of taxes more uniform.

Implementation Considerations

This bill would improve the department's operations by eliminating an area of taxpayer error and confusion.

If this bill is adopted, some taxpayer education and changes to tax booklets and instructions would be required so taxpayers and tax preparers will be aware of the change in the due date of the LLC minimum tax. These changes can be handled during the department's normal annual updates.

FISCAL IMPACT

Departmental Costs

By reducing taxpayer errors, this bill may result in a minor but undeterminable savings of departmental costs.

Tax Revenue Estimate

Based on data and assumptions discussed below, this bill would result in revenue losses as shown below.

Estimated Revenue Impact of AB 190
(In $Millions)
Enactment Assumed After 4/15/99

Fiscal Years	1999/00	2000/01	2001/02
Revenue Impact	(15)	(1)	(1)

This revenue estimate does not take into account any possible changes in employment, personal income, or gross state product that might result from this measure.

Tax Revenue Discussion

This bill is essentially a timing issue and would not affect the total amount of state income tax revenue received over the long run, but would result in the one-year deferral of $15 million. However, the year in which the deferral occurs would depend upon the enactment date of this bill.

This bill would result in the delayed receipt of revenue as shown below. This bill would defer the receipt of $15 million in revenues from the 1999/2000 fiscal year to 2000/2001, resulting in a $15 million deferral for 1999/2000. Additional deferrals of $1 million are assumed due to growth of new LLCs that would otherwise pay taxes in an earlier fiscal year. A growth rate of 5% was used to calculate the growth of LLC formation.

Tax Revenue Estimate Recap

	Assembly Bill 1208 (As Amended July 1 1999)		**Personal Income Tax**			**Bank & Corporation Tax**		
			(in millions)			**(in millions)**		
	Description		**1999-0**	**2000-1**	**2001-2**	**1999-0**	**2000-1**	**2001-2**
1	Exclusion of value of meals to employee		-$1	-$1	-$1	-	-	-
2	Employer Deductions for Vacation and Severance Pay	a/	Minor Gain	Minor Gain	Minor Gain	$2	$3	$3
3	Certain Trade Receivables Ineligible for Mark-To-Market Treatment		Minor Gain	Minor Gain	Minor Gain	$12	$18	$18
4	Exclusion-Min. Req. Distributions from AGI for Roth IRA Conversions	b/	-	-	-	-	-	-
5	Farm Production Flexibility Contract Payments		Insignificant	Insignificant	Insignificant	Insignificant	Insignificant	Insignificant
6	Certain Deductible Liquidating Distributions of RICs & REITs	c/				$40	$5	-
7	Tax Treatment of Cash Options for Qualified Prizes		Minor Loss	Minor Loss	Minor Loss	-	-	-
8	Exclusion from Income for Employer-Provided Transportation Benefits		Insignificant	Insignificant	Insignificant	Insignificant	Insignificant	Insignificant
9	Payments Received Pursuant to the Ricky Ray Hemophilia Relief Fund Act		Insignificant	Insignificant	Insignificant	-	-	-
10	Waiver of Estimate Tax Penalty		No Impact	No Impact	No Impact	No Impact	No Impact	No Impact
11	1998 Federal Technical Changes		Insignificant	Insignificant	Insignificant	Insignificant	Insignificant	Insignificant
12	Deleted		-	-	-	-	-	-
13	B & C Section 179 Expensing Allowance		-	-	-	-$36	-$28	-$27
14	Profit Split Method		-	-	-	-$1	-$3	-$2
15	Capital Loss Carry-overs	d/	-	-	-	-$5	$1	$3
16	LLC Annual Franchise Tax Due Date	e/				-$15	-$1	-$1
	TOTALS		-$1	-$1	-$1	-$3	-$5	-$6
	Minor = Loss or gain of less than $500,000							
a/	Baseline revenue gains are projected to be $65 million for 1999-0 and $3 million thereafter.							
b/	Baseline revenue gains are projected to be $84 million for 2004-5, $101 million for 2005-6, and $99 million for 2006-7.							
	Conformity gains are esstimated to be $1 million annually beginnning with the fiscal year 2004-5.							
c/	Baseline revenue gains are projected to be $15 million annually beginning in 1998-9,							
d/	Assumes Regulation 25106.5 is in place.							
e/	This provision is a timing issue and would not affect the total amount of state income tax revenue received over the long run, but would result in one-year deferral of $15 million							

BOARD POSITION

Support

On July 6, 1999, the Franchise Tax Board voted 2-0 to support the June 29, 1999, version of this bill. In addition, the Board previously voted to sponsor item 16, which was added by the July 1, 1999, amendment.